

# Raising Seed Capital From the Rest of Us

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## INTRODUCTION

When a business client approaches its attorney, wanting to raise capital from unaccredited investors, the attorney's most common response is, "I don't recommend it." Most business attorneys recommend that the client use SEC Rule 506 (17 CFR §230.506), limit the offering to accredited investors only, and use an investor questionnaire to make sure that all offerees are accredited. For some clients, however, this is not a practical option because there are no (or too few) accredited investors interested in the opportunity. Even before the definition of "accredited investor" was narrowed by the Dodd-Frank Wall Street Reform and Consumer Protection Act (Pub L 111-203, 124 Stat 1376), it was estimated that only 8 percent of the population meets the definition. SEC Release No. 33-8766; IA-2576; File No. S7-25-06, available at <http://www.sec.gov/rules/proposed/2006/33-8766.pdf>.

Moreover, the client may have a very good reason for wanting to raise capital from unaccredited investors. For example, a company that sells consumer goods may be interested in having its customers as investors because customers who are investors are likely to increase their purchases from the company. This is exactly what happened when Real Goods (see <http://www.realgoods.com/>) sold shares to its customers in a direct public offering. Customers who became investors doubled their average purchases from the com-

pany. See <http://www.dfdpo.com/clientsum5.htm>.

This article discusses some of the options available to businesses that would like to solicit investors from a broader pool—from the 92-plus percent of us who do not meet the SEC's definition of "accredited investor."

## NON-SECURITIES OFFERINGS

One of the easiest ways to raise money from unaccredited investors is to structure the offering in such a way that the federal and state securities laws do not apply. To accomplish this, the attorney must be very familiar with the (very broad) definition of a "security" under federal and state law. If an interest or instrument does not meet the definition, there is no need to comply with the securities laws.

The term "security" is defined in the federal Securities Act of 1933 (1933 Act) (15 USC §§77a-77aa) as follows (15 USC §77b(a)(1) (emphasis added)):

any note, stock, treasury stock, security future, security-based swap, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, *investment contract*, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, any put, call, straddle, option, or privilege on any security, certificate of deposit, or group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities

exchange relating to foreign currency, or, in general, any interest or instrument commonly known as a “security”, or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.

**NOTE:** The Securities Exchange Act of 1934 (1934 Act) (15 USC §§78a–78pp) also contains a definition of “security.” See 1934 Act, §3(a)(10) (15 USC §78c(a)(10)). Although it differs slightly from the 1933 Act definition above, in *Tcherepnin v Knight* (1967) 389 US 332, 335, 19 L Ed 2d 564, 88 S Ct 548, the Supreme Court called the two definitions “virtually identical.” For the definition of “security” under the California blue-sky laws, see Corp C §25019.

Over the years, many schemes for raising capital have been devised in attempts to avoid application of the securities laws. These schemes have been analyzed by the courts to determine whether they are “investment contracts,” and therefore “securities” under 15 USC §77b(a)(1). The leading case on the definition of an investment contract is the U.S. Supreme Court case, *SEC v W.J. Howey Co.* (1946) 328 US 293, 90 L Ed 1244, 66 S Ct 1100. Under the *Howey* test, an investment contract is “a contract, transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party.” 328 US at 298.

The “investment of money” prong of the *Howey* test requires that the investor commit his or her assets to the enterprise in such a manner as to subject the investor to financial loss. *El Khadem v Equity Secs. Corp.* (9th Cir 1974) 494 F2d 1224, cert denied (1974) 419 US 900. The U.S. Supreme Court has defined “profits” as “either capital appreciation resulting from the development of the initial investment . . . or a participation in earnings resulting from the use of investors’ funds.” *United Hous. Found., Inc. v Forman* (1975) 421 US 837, 852, 44 L Ed 2d 621, 95 S Ct 2051. The promised return may be fixed or variable and may be marketed as low-risk or “guaranteed.” *SEC v Edwards* (2004) 540 US 389, 394, 157 L Ed 2d 813, 124 S Ct 892.

Although the definition of “security” is very broad, there are certain ways that businesses can raise money without offering investment opportunities that fall within the definition of a security. Several of these alternatives are discussed below.

### Donations

A security creates an expectation that the investor will receive a financial return. If someone gives money to a business with no expectation of a return, the securities laws and regulations do not apply. Many entrepre-

neurs (as well as charitable organizations) are using so-called crowdfunding websites such as Kickstarter.com (see <http://www.kickstarter.com/>) and Indiegogo.com (see <http://www.indiegogo.com/>) to raise money for various causes. Entrepreneurs who solicit donations often provide nonmonetary rewards to donors. For example, a recent successful fund-raising effort on Kickstarter for the reopening of the New Parkway Theater in Oakland offered the following:

- Pledge \$25 or more: Five free tickets to the New Parkway Theater.
- Pledge \$50 or more: Two free tickets to the theater, a pitcher of beer, a pizza, and a reserved loveseat.
- Pledge \$100 or more: Ten free tickets and a +1 pass to the Grand Reopening Party.
- Pledge \$500 or more: One free-movie pass for an entire year and a +1 pass to the Grand Reopening Party.
- Pledge \$1000 or more: One reserved screening room at the theater for one night for a double feature, together with 10 pitchers of beer and 10 pizzas.
- Pledge \$2500 or more: Lifetime free-movie pass and a +1 pass to the Grand Reopening Party.
- Pledge \$5000 or more: Two lifetime free-movie passes (including 2 passes to the Grand Reopening Party) and a reserved loveseat every time the donor would like to come to the movies.

This campaign raised \$56,832, exceeding the amount needed to reopen the theater.

At what point might a reward be valuable enough that it could be seen as a financial return on investment? This issue has yet to be tested, but it is advisable to make sure that any rewards offered are valued at no more than the amount donated.

**NOTE:** The courts have held that the “investment” prong of the *Howey* test may be satisfied by the investment of something other than cash, such as goods or services. See, e.g., *International Bhd. of Teamsters v Daniel* (1979) 439 US 551, 58 L Ed 2d 104, 99 S Ct 71. However, payment of “profits” in something other than cash has not been addressed by the courts. Dicta in *United Hous. Found., Inc. v Forman* (1975) 421 US 837, 44 L Ed 2d 621, 95 S Ct 2051, imply that noncash “rewards” could be excluded from the definition of profits if they are not easily convertible into cash (421 US at 855):

The Court of Appeals also found support for its concept of profits in the fact that Co-op City offered space at a cost substantially below the going rental charges for comparable housing. Again, this is an inappropriate the-

ory of “profits” that we cannot accept. . . . This benefit cannot be liquidated into cash.

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### Preselling

The U.S. Supreme Court has stated that “[w]hat distinguishes a security transaction . . . is an investment where one parts with his money in the hope of receiving profits from the efforts of others, and not where he purchases a commodity for personal consumption.” *United Hous. Found., Inc. v Forman* (1975) 421 US 837, 858, 44 L Ed 2d 621, 95 S Ct 2051. This distinction can be used to avoid coverage of the securities laws. For example, two entrepreneurs wanted to open a high-quality, environmentally responsible café in downtown Oakland. They got the word out to the community about their idea, and then sold “Café Creator” cards, which were gift certificates to the yet-to-open café. The cards entitled purchasers to café products valued at more than the purchase price of the card. For example, a \$1000 card entitled the holder to \$1200 worth of purchases once the café opened. Arguably, because the entrepreneurs were selling gift certificates for coffee and pastries and not an investment with an expectation of a monetary return, the Café Creator cards were not securities.

### Memberships

A membership that a business sells to raise funds may also be a “commodity for personal consumption” within the meaning of the *United Hous. Found.* case. Many nonprofit organizations use this model, and for-profit businesses can do the same. Members may receive benefits such as T-shirts, product discounts, or exclusive invitations to events, but have no rights, obligations, or ownership interest conferred by the statute governing the entity (corporation, LLC, or other entity).

### Return of Principal Only

If an issuer promises to return nothing more than the original investment amount, without any additional dividend, interest, or appreciation in value, the instrument being offered is not a security. This is how Kiva, the popular microfinance website (see <http://www.kiva.org/>), avoids having to comply with securities laws.

### Product Discounts

Companies like Costco Wholesale Corporation (Costco) sell memberships in exchange for product discounts received at the time of purchase. Another interesting model is REI, the successful outdoor equipment chain. REI is a consumer cooperative that sells memberships to its customers. See <http://www.rei.com/aboutrei/business.html>. At the end of the year, REI members receive a “dividend” based on the amount spent at REI during the year. REI takes the position that its memberships are not securities because what members are really buying is the right to receive discounts on the items they purchase—not at the time of purchase as at Costco, but at the end of the year in the form of a rebate check.

### PRIVATE OFFERINGS

Although there have been some great success stories, raising money for new businesses without offering interests that fall within the definition of a security is not easy. Most people want to receive a return on their investment in cash. There are ways to conduct private offerings that allow issuers to solicit unaccredited investors. Most business lawyers are familiar with these, but it is worth reviewing them in the context of some examples.

#### Corporations Code §25102(f)

The California §25102(f) private offering exemption to the qualification requirement (see Corp C §§25102(f), 25110) can be used to raise capital from up to 35 unaccredited investors that meet certain requirements. The following are the requirements for the offer and sale of a security to be eligible for the §25102(f) exemption:

- The offering can be made to an unlimited number of “excluded purchasers,” as defined in 10 Cal Code Regs §260.102.13.
- “Excluded purchasers” include officers and directors of the company, a person who works for the company who has executive-level duties and authority, and accredited investors. See 10 Cal Code Regs §260.102.13.
- The offering can be made to a maximum of 35 purchasers who do not meet the definition of an “excluded purchaser” if they meet one of the following requirements (Corp C §25102(f)(1)–(2)):
  - They have a preexisting personal or business relationship with the company or its principals; or
  - They have the ability to protect their interests due to their financial experience or the fact that they have experienced professional advisors.

- All purchasers must represent that they are purchasing for their own account and not for resale. Corp C §25102(f)(3).
- The offering of the security may not be advertised to the public. Corp C §25102(f)(4).

#### “Preexisting Personal or Business Relationship”

The term “preexisting personal or business relationship” includes any relationship consisting of personal or business contacts of a nature and duration such as would enable a reasonably prudent purchaser to be aware of the character, business acumen, and general business and financial circumstances of the person with whom such relationship exists. 10 Cal Code Regs §260.102.12(d)(1).

Unfortunately, there is not much guidance on what qualifies as a sufficient preexisting personal or business relationship or sufficient financial experience to meet the requirements of Corp C §25102(f). Interpretations of these requirements by California courts have been mainly in the context of criminal prosecutions for fraudulent sales of securities. For example, in *People v Simon* (1995) 9 C4th 493, 503, n8, 37 CR2d 278, the California Supreme Court stated that:

[t]he relationship described in the rule contemplates more than mere acquaintance. If the qualification requirement is to serve the purpose of the corporate securities law, which is to protect unsophisticated investors [citation omitted], the relationship must be one of sufficient duration and nature that the offeror of a security has reason to believe the investor is able to assess the issuer’s honesty and competence. . . . Whether a prior relationship warranting reliance on the seller of an unregistered security exists is an objective test and looks to what a reasonably prudent investor would be aware of about the offeror from the prior personal or business relationship. This test is intended to protect investors by placing on the offeror the burden of establishing that the nature and duration of the relationship is one that would enable a reasonably prudent investor to assess the general business and financial circumstances of the issuer.

Further, in *People v Park* (1978) 87 CA3d 550, 565, 151 CR 146, the court stated that “it is unquestionable that occasional meetings between the offeror and offerees without demonstrating the true nature of the relationship between them, do not satisfy the regulatory condition for private exemption.”

#### “Financial Experience”

In *People v Graham* (1985) 163 CA3d 1159, 1172, 210 CR 318, the court stated that the financial experience of the offeree should be measured

from the issuer’s rather than the offeree’s point of view... [because] that approach...is more consistent with the statutory purpose of protecting the gullible investor [citations omitted]

because it places on the issuer the burden of establishing his offerees’ abilities to “fend for themselves” as a condition for exemption from the regulatory provisions that would otherwise apply.

Courts have implied that qualifications such as prior investment experience in similar ventures, serving as a board director, operating a corporate enterprise, or a degree in business administration could be sufficient to satisfy the “financial experience” test. See, e.g., *Stewart v Ragland* (9th Cir 1991) 934 F2d 1033; *People v Salas* (2006) 37 C4th 967, 38 CR3d 624.

Mill Valley Beerworks, a successful brew pub in Mill Valley, relied on the §25102(f) exemption to raise almost \$200,000 in capital needed to open the business. The owners used a creative pitch to people they knew in their community: Sponsor one bottle of beer for \$5000 and receive a note paying 10-percent interest. In addition, for each beer bottle sponsored, the company donated \$250 to a charity chosen by the investor.

**NOTE:** Of course, an issuer relying on the Corp C §25102(f) state private-offering exemption must also identify, and qualify under, an exemption under the federal securities laws.

### Private Placements Under Regulation D

The federal SEC Regulation D (17 CFR §§230.501–230.508) provides three different exemptions from the federal securities registration requirements of the 1933 Act. Each one allows for inclusion of unaccredited investors in the offering. The requirements for each exemption are summarized briefly below. For a more extensive discussion of SEC Regulation D, see *Financing and Protecting California Businesses*, chap 6 (Cal CEB 2006).

#### Rule 504

Rule 504 (17 CFR §230.504) was promulgated under the SEC’s authority granted by §3(b) of the 1933 Act (15 USC §77c(b)) to provide for exemptions from registration for small offerings. Rule 504 can be used to raise up to \$1 million. Unlike the other two rules under Regulation D, the issuer is not required to furnish any particular information to potential investors who are unaccredited, but the issuer should provide a private placement memorandum containing sufficient information to allow potential investors to make an informed investment decision. See 17 CFR §230.502(b). There is no limit on the number of unaccredited investors that may invest in an offering under Rule 504.

Of course, the issuer must still comply with applicable state securities laws. In the case of a California of-

fering, the issuer would likely rely on Corp C §25102(f), discussed above, which would limit the number of unaccredited investors to 35.

#### Rule 505

Rule 505 (17 CFR §230.505) was also promulgated under §3(b) of the 1933 Act (15 USC §77c(b)). It can be used to raise up to \$5 million. Under both Rule 505 and Rule 506, there are extensive requirements concerning the information that must be provided to unaccredited investors. 17 CFR §230.502(b). This information can be onerous to prepare but might be worth the effort if there are a significant number of potential unaccredited investors for an offering. Under Rule 505, the issuer will also need to comply with applicable state securities regulations.

#### Rule 506

Unlike Rules 504 and 505, Rule 506 (17 CFR §230.506) was promulgated under §4(2) of the 1933 Act (15 USC §77d(2)), the private placement exemption. Rule 506 can be used to raise an unlimited amount and, under the National Securities Markets Improvement Act of 1996 (Pub L 104–290, 110 Stat 3416), the issuer need not identify an exemption from state qualification (although states may require notice filings and fees). Under Rule 506, there may be no more than 35 unaccredited investors, and an unaccredited investor must “either alone or with his purchaser representative(s) ha[ve] such knowledge and experience in financial and business matters that he is capable of evaluating the merits and risks of the prospective investment.” 17 CFR §230.506(b)(2)(ii).

#### A Case Study

Gather Restaurant in Berkeley, whose chef was named chef of the year in Esquire Magazine, would not be here today without creative use of Regulation D. It started with a traditional private capital-raising campaign in which only accredited investors were approached. The business was well on its way to meeting its goal when the events of October 2008 hit. Suddenly, investors were more cautious and Gather’s capital-raising efforts stalled. The founders learned that under Regulation D, they could solicit unaccredited investors as long as they met the information requirements. The ability to solicit unaccredited investors under Rule 505 allowed Gather to meet its fundraising goals. It now has over 60 investors representing a total investment of more than \$2 million, with investments ranging in size from \$2750 to over \$400,000.

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### COOPERATIVES

Cooperatives are businesses formed under state cooperative statutes, which generally conform to the following principles:

- Cooperatives are set up to benefit the people who do business with the cooperative (known as patrons), *e.g.*, the consumers who purchase from the cooperative, the farmers who market products through the cooperative, or the employees who work for the cooperative.
- The patrons of the cooperative who become members (usually by paying a membership fee or making a capital contribution) each have one vote, regardless of the amount of capital each member has contributed to the cooperative.
- Surplus revenue (after expenses and operating reserves) are refunded to the members in proportion to their patronage of the cooperative. Their patronage may be determined based on the value or volume of purchases made from the cooperative, products marketed through the cooperative, or labor contributed to the cooperative.

California has a cooperative statute, codified at Corp C §§12200–12704.

Why a discussion of cooperatives in an article about raising capital from unaccredited investors? Because in many cases cooperative memberships do not fall within the definition of a security, and even if they do, most states exempt cooperative memberships, either partially or completely, from the securities offering qualification requirement. See, *e.g.*, Corp C §25100(r). Thus, cooperatives can be a vehicle for raising capital from the public.

Whether a membership in a cooperative is considered a security will depend on whether the membership has the characteristics associated with a security discussed above. When members pay a membership fee primarily to receive the benefits of membership and not to receive

a financial return, the membership generally will not be a security. See, e.g., *United Hous. Found., Inc. v Forman* (1975) 421 US 837, 856 n21, 44 L Ed 2d 621, 95 S Ct 2051; *Grenader v Spitz* (2d Cir 1976) 537 F2d 612; *Rosenberg & Sons, Inc. v St. James Sugar Cooperative, Inc.* (DC La 1976) 447 F Supp 1. As noted above, REI does not believe that its memberships are securities because the patronage dividends are characterized as refunds rather than a financial return on an investment. Each cooperative must carefully consider whether its memberships might fall under the definition of securities.

In California, Corp C §25100(r) exempts from the securities offering qualification requirement

any shares of memberships issued by [a California cooperative corporation], provided the aggregate investment of any shareholder or member in shares or memberships sold pursuant to this [exemption] does not exceed three hundred dollars (\$300).

This exemption does not apply to (Corp C §25100(r))

the shares or memberships of that corporation if any promoter thereof expects or intends to make a profit directly or indirectly from any business or activity associated with the corporation or the operation of the corporation or from remuneration, other than reasonable salary, received from the corporation.

It also does not apply to nonvoting shares or memberships. Thus, a business formed under the California cooperative statute can offer memberships to the public without qualifying the offering, so long as the maximum investment of each member never exceeds \$300.

Many states offer much broader exemptions. For example, in Colorado, “[a]ny security . . . issued or sold by a cooperative association as an investment in its stock or capital to the members of a cooperative association . . . is exempt from securities laws as contained in [the Colorado Securities Act]. Such securities . . . may be sold lawfully by the issuer or its members or salaried employees without the necessity of being registered as a broker or dealer.” Colo Rev Stat 7–55–115.

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Of course, it will be necessary to identify an appropriate federal securities law exemption. There is no federal exemption from the registration requirement for cooperative memberships, except for certain kinds of agricultural cooperatives. See §3(a)(5)(B)(i) of the 1933

Act (15 USC §77c(a)(5)(B)(i)). However, in many cases, cooperatives may use the federal intrastate exemption. See §3(a)(11) of the 1933 Act (15 USC §77c(a)(11)).

In addition to memberships, cooperatives can offer other kinds of investment opportunities, such as preferred nonvoting shares or notes. These instruments are almost certainly securities. See, e.g., *Reves v Ernst & Young* (1990) 494 US 56, 108 L Ed 2d 47, 110 S Ct 945.

### **DIRECT PUBLIC OFFERINGS**

Suppose your client wants to be able to offer a financial return, does not have preexisting relationships with enough potential investors to do a private offering, and does not want to form as a cooperative? The next option is to conduct a public offering. Unlike an initial public offering (IPO), which only makes financial sense for offerings of at least \$25 million, your client can conduct a direct public offering (DPO), also known as a self-underwritten offering. The term DPO does not have a precise legal definition, but it is used in this article to mean any type of securities offering in which the offeror solicits the public generally rather than a limited number of unaccredited investors.

There are several legal ways to conduct a DPO. These include:

- A full federal registration using Form S-1 and qualification by coordination in all of the states where the offering will be made;
- An offering under Regulation A and state-level qualification by coordination;
- A state-level qualification in conjunction with the federal intrastate exemption; or
- A single or multi-state offering under Rule 504 plus state-level qualification.

The first two options are fairly well known to the business law practitioner. The second two are less commonly used and are briefly described below.

#### **California Qualification in Conjunction With the Federal Intrastate Exemption**

For an offering to be eligible for the intrastate exemption (§3(a)(11) of the 1933 Act (15 USC §77c(a)(11))), all investors must reside in a single state and the issuer must be incorporated in and doing most of its business in that state. If the securities are offered, sold, or re-sold within 9 months of the initial offering to even one out-of-state investor, the exemption may be lost.

The best way to ensure compliance with §3(a)(11) is to take advantage of the safe harbor provision in SEC Rule 147 (17 CFR §230.147). The conditions required to meet the safe harbor are as follows:

- 80 percent of the issuer's assets are located in the state in which the offering is made;
- 80 percent of the issuer's revenue comes from the state in which the offering is made; and
- 80 percent of the proceeds from the offering will be used within the state in which the offering is made.

The intrastate exemption is self-executing; there are no required federal filings.

If an offeror qualifies for the federal intrastate exemption, it is still necessary to obtain a qualification under the California state securities laws. See Corp C §§25000–25707. A discussion of the mechanics of a California qualification is beyond the scope of this article, but many companies have successfully used this route to raise capital in California from the public. Note, however, that if the issuer does not have a history of profitable operations, the California Department of Corporations may impose suitability requirements with respect to the offerees. See 10 Cal Code Regs §260.140.01.

#### California or Multi-State Offering in Conjunction With Rule 504

As discussed above, Rule 504 (17 CFR §230.504) is an exemption from the federal registration requirement that allows a company to offer up to \$1 million of securities in a private placement. But Rule 504 has another aspect that many attorneys are less familiar with: Used in conjunction with state-level qualification, Rule 504 can be used to conduct a DPO. If the offeror qualifies the offering under the securities law of a state that requires the public filing and delivery to investors of a substantive disclosure document—and most states do—Rule 504 allows the offering to be made to the public in the state where the registration was completed. See 17 CFR §230.504(b)(1)(i).

What if the offeror does the state-level compliance work to offer the securities in New York—a state where the securities laws do not require the public filing and delivery to investors of a substantive disclosure document? In that case, the offeror may complete the registration process in a state that does have these requirements and then deliver the disclosure document that was prepared for that state to *all* potential investors. See 17 CFR §230.504(b)(1)(ii).

#### SCOR Form

Both the Rule 504 exemption and the intrastate exemption can be used in conjunction with state registration accomplished through the use of a Small Company Offering Registration (SCOR) form (NASAA Form U-7), developed by the North American Securities Admin-

istrators Association (NASAA) and available at [http://www.nasaa.org/Industry\\_Regulatory\\_Resources/Corporation\\_Finance/564.cfm](http://www.nasaa.org/Industry_Regulatory_Resources/Corporation_Finance/564.cfm). California does accept the SCOR form, although California is considered to be a less friendly state for SCOR offerings.

The benefit of using the SCOR form is that it simplifies multi-state offerings because the form is accepted in most states. Many states participate in regional coordinated review of SCOR offerings. An offeror that requests coordinated review will generally only have to work with one of the states in the region, the lead jurisdiction, which will coordinate the review and comments of all states within the region.

The following is a list of the groups of states that do coordinated review:

- **CR-SCOR-Mid-Atlantic:** Delaware, Maryland, New Jersey, Pennsylvania, Virginia, and West Virginia
- **CR-SCOR-Midwest:** Illinois, Indiana, Iowa, Kansas, Michigan, Minnesota, Missouri, Nebraska, North Dakota, South Dakota, and Wisconsin
- **CR-SCOR-New England:** Connecticut, Maine, Massachusetts, New Hampshire, Rhode Island, and Vermont
- **CR-SCOR-Southwest:** Arkansas, Oklahoma, Texas
- **CR-SCOR-West:** Alaska, Arizona, Colorado, Idaho, Montana, Nevada, New Mexico, Oregon, Utah, Washington, and Wyoming

#### CONCLUSION

Raising seed capital from unaccredited investors for a new business venture without violating the securities laws is tricky. The penalties for violation of those laws can be severe. At a minimum, the client may be forced to return all the money received from investors, long after the money has been spent, and damages in cases involving securities fraud can be much greater. It is essential for counsel to perform a careful analysis of possible alternatives for the client and to plan the fund-raising effort with care.

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